Barriers to Business Expansion in Malawi's New Policy Environment

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Abstract

This paper addresses the need for prioritizing constraints facing the Malawi private sector, examines the sector's environment and identifies the most important problems perceived by firms as impeding their expansion. It is based on a study conducted in 1999 by Associates for International Resources and Development (AIRD) in partnership with Millennium Consulting Group and the Malawi Investment Promotion Agency (MIPA)[1].

The survey and analysis of this report are exploratory since the sample was small and the resources too limited to do an extensive examination. The primary value of the study, however, is that it asks the private sector what it thinks are its major constraints, prioritizes these and measures their magnitude to the extent possible, analyzes the most important of these constraints, and recommends ways in which they might be overcome.

[1] MIPA is a parastatal mandated by the Investment Promotion Act of 1991 to promote, encourage, attract, and facilitate local and foreign investment.

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I. INTRODUCTION

Under its various trade liberalization programs, Malawi has put considerable emphasis on the private sector as the engine for growth and development. However, despite a reformed policy environment, private enterprises, especially those of small and medium size, find it difficult to take advantage of the new opportunities. The constraints cited are numerous and include: unpredictable macroeconomic environment; lack of working capital and medium-term finance; restrictive hiring and firing regulations; increased competition from cheap imports; inadequate telecommunications infrastructure; a legal, regulatory, and judicial environment that is slow, costly and uncertain; limited market opportunities; costly and often monopolized transportation services; high levels of taxation; and inadequate access to reliable power and water.

The wide range of problems encountered by firms makes it very difficult for donors and governments to define priorities for reform. As a result, USAID/Malawi and the Malawi Investment Promotion Agency (MIPA) expressed interest in assessing the severity of these problems for different types of firms in order to identify the constraints that should be addressed first. Particular emphasis was placed on exporting firms or those with a potential to export, since Malawi, like most other developing countries, has to diversify its export base and venture into new activities in which it has a comparative advantage in order to achieve sustainable growth. The need to diversify away from its major agricultural exports -- tobacco, sugar, tea, and cotton -- arises from a number of factors including deteriorating terms of trade, detrimental effects on tobacco exports of the anti-smoking lobby in the west, and fluctuations in world market prices. In addition to promoting growth, increased manufacturing activities should also result in greater job opportunities, thereby contributing positively toward the alleviation of the country's poverty.

This paper addresses the need for prioritization of constraints facing the private sector by examining the environment within which the sector operates and by conducting a quantitative survey to identify the most important problems perceived by firms as impeding their expansion. The paper is based on a study conducted in 1999 by Associates for International Resources and Development (AIRD) in partnership with Millennium Consulting Group and the Malawi Investment Promotion Agency (MIPA)[2].

The next section of the paper looks at the background of the Malawian economy, and especially its macroeconomic performance during the period 1992-98. This is followed by a discussion of the methodology used in the survey and a description of the sample. There is then a detailed discussion of the constraints faced by the private sector in Malawi, based partly on the survey and partly on informal interviews, government documents, and other sources of information. The final section presents the conclusions and policy recommendations of the study.

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[2] MIPA is a parastatal mandated by the Investment Promotion Act of 1991 to promote, encourage, attract, and facilitate local and foreign investment.

II. BACKGROUND

A. Overview of the Economy

Malawi emphasized maintaining macroeconomic stability and growth of infrastructure and estate agriculture as the main elements of its development strategy after it attained its independence in 1964. Poverty was to be dealt with by a "trickle down effect". This strategy proved effective in promoting growth and macroeconomic stability, but did not translate into notable improvements in the living conditions of the average Malawian.

During the 1960s and 1970s, real gross domestic product (GDP) more than doubled and per capita income increased by 3 percent per year. However, since structural weaknesses persisted and the economic base remained narrow – tobacco continued to be the dominant product, accounting for more than 70 percent of export earnings - the economy remained highly vulnerable to external shocks. Much of the growth momentum was lost in the 1980s, when a series of destabilizing factors came into play. These included declining tobacco prices in the international market and the civil strife in Mozambique, which increased international transportation costs and brought large numbers of refugees and security related expenditures.

Since the mid-1990s, Malawi has been implementing a series of broad programs of macroeconomic adjustment and structural policy reform supported by substantial external financial and technical assistance from the International Monetary Fund (IMF), the World Bank, and other donors. The objective of these programs has been to liberalize the economy and promote development through growth of the private sector. The reform programs have included elimination of price controls and quantitative trade restrictions, replacement of fixed exchange rates punctuated by discrete devaluation with managed floatation of the exchange rate, liberalization of the agricultural market, rationalization of the civil service, and privatization of public enterprises.

Despite the persistent pursuit of structural adjustment, the economy remains very fragile, narrowly based, and lacking in key social services and infrastructure. Agriculture still provides employment and subsistence for some 80 percent of the population and contributes approximately 36 percent of GDP and 85 percent of export earnings. After more than a decade of stabilization and adjustment, the structure of the economy is still dominated by the production, processing, and distribution of a limited number of agricultural crops (mainly tobacco, tea, sugar, cotton, and maize – the dominant food staple), as shown in Table 1. Furthermore, agricultural production remains totally dependent on erratic climatic conditions.

Malawi is one of the most densely populated countries in Africa, with an average of 171 persons per square kilometer of arable land. Population growth estimated at 3.2 percent annually is exerting strong pressure on the stock of arable land, which constitutes only 48 percent of the total land area.[3] During the last two decades, average landholding size decreased by 50 percent. At present, smallholder households with landholding sizes larger than 2 hectares constitute a mere 12 percent of all farming households. The agriculture sector is thus experiencing difficulty in

[3] E.I.U, *Country Profile Malawi 1991-1998*.

generating sufficient income and employment opportunities for a rapidly growing labor force, while the entire formal sector is able to absorb no more than one-quarter of the growth in the number of those seeking jobs.

Table 1: Exports by Main Commodity, 1994-98 (% share of total value)

	1994	**1995**	**1996**	**1997**	**1998**
Tobacco	62.1	65.3	64.1	59.8	57.7
Tea	9.6	6.9	5.5	12.5	11.8
Sugar	8.2	6.8	7.3	5.3	6.6
Cotton	0.6	1.0	3.2	5.3	6.6
Rice	0.7	0.4	0.3	0.3	0.4
Coffee	4.7	4.0	2.3	2.2	2.3
Pulses	0.9	1.9	2.6	1.3	1.7
Maize	0.6	1.3	-	-	-
Other	12.6	12.4	14.8	13.3	14.4
Total	100.0	100.0	100.0	100.0	100.0

Source: Economic Report 1998

Limited access by most of the rural population to productive assets, including land, modern technology, and financial capital, suggests that any further contribution by agriculture to income and employment is rapidly approaching its limits.

B. Macroeconomic Performance, 1992-1998

There has been substantial unevenness in both the year to year and the sectoral performance of Malawi's economy. Table 2 presents GDP data by sector of origin between 1992 and 1997. Economic performance as measured by growth in real GDP declined by 12.4 percent in 1994, compared with growth of 10.8 percent in 1993. The drop in 1994 was mainly attributed to poor performance of the agricultural sector, which declined by 29.7 percent in 1994 owing to the severe drought experienced in most parts of the country. The decrease in small-scale agriculture was particularly steep at 33.5 percent, in comparison with large-scale agriculture, which declined by 19.1 percent. There was substantial improvement in economic performance in 1995, with real GDP growing by 9.0 percent following the drought of the previous year. In 1996, real GDP rose strongly again by 9.5 percent, followed by a rate of growth of 5.2 percent in 1997.[4] While GDP growth rate was mainly attributed to increases in agricultural productivity, it was also the result of growth in the distribution sector, estimated at 12.4 percent in 1997. Manufacturing, on the other hand, remained stagnant, signifying that economic activity in Malawi is concentrated in agriculture and trade rather than in manufacturing.

The uneven economic performance of Malawi, especially in manufacturing, can partly be blamed on its poor macroeconomic environment. High rates of inflation and unstable exchange rates have meant that returns on private sector activities are uncertain. As shown in Table 3, annual inflation as measured by the national retail price index increased from 22.8 percent in 1993 to

[4] International Monetary Fund, *Malawi – Recent Economic Developments*, IMF Staff Country Report No. 97/107, October 1997; Government of Malawi, *Economic Report 1998*.

34.6 percent in 1994. This rise reflected the monetary imbalances in the economy and the cost-push pressure triggered by the depreciation of the kwacha following its floatation in February 1994. Inflationary pressure was further fueled by food shortages arising from the drought. In 1995, annual inflation

Table 2: GDP by Sector of Origin
1978 Constant Factor Cost (MK million)

	1992	**1993**	**1994**	**1995**	**1996**	**1997**
Agriculture	275.2	421.0	297.6	381.8	493.2	521.2
Small-scale	168.3	311.1	206.9	277.1	387.4	409.1
Large-scale	106.9	109.9	90.7	104.7	105.9	112.1
Manufacturing	141.6	126.8	130.8	139.1	131.3	138.0
Electricity and Water	26.3	27.2	29.3	30.2	29.8	31.8
Construction	43.0	41.2	39.8	41.5	46.1	49.1
Distribution	129.5	118.4	112.6	114.7	128.8	136.5
Transport and Communication	59.4	56.7	51.8	53.2	57.1	61.2
Financial and Prof. Services	71.4	67.3	62.3	66.5	71.3	75.9
Ownership of Dwellings	44.4	44.9	45.9	47.0	48.2	49.3
Private, Social Services	44.9	45.1	46.4	47.4	48.4	49.5
Producer of Government Services	154.8	154.2	147.3	142.0	146.5	155.5
Unallocable Finance Charges	-25.7	-11.5	-25.4	-64.0	-50.0	
GDP at Factor Cost	972.2	1,076.9	952.1	1,038.0	1,136.8	1,218

Source: Economic Report 1997 and 1998

rose to 83.3 percent. The general trend in the inflation rate from the second quarter of 1995 indicated a steady decline, however, and in 1996 the annual rate of inflation came down to 37.6 percent. It dropped to single digits the following year because of greater food availability and stability in the exchange rate, only to rise rapidly again in 1998 due to a shortage of food and depreciation of the kwacha against other currencies. Such high and variable rates of inflation preclude accurate business planning and create high interest rates, which increases the cost of investment and business operations.

Table 3: Annual Inflation Rates

Year	Rates
1993	22.8
1994	34.6
1995	83.3
1996	37.6
1997	9.2
1998	29.8 (projected)

Source: Monthly Statistical Bulletin, National Statistical Office, February 1998

In addition to high inflation, management of foreign exchange has generally been ineffective. The regime of fixed nominal exchange rates punctuated by discrete devaluation was replaced by a managed floatation of the exchange rate in 1994. But nominal exchange rates continue to be unstable and unpredictable. Periods of stable nominal exchange rates and sustained appreciation of the real exchange rate have given way to sudden and large discrete changes. As an example, in August 1998, the kwacha was devalued by about 60 percent to reach an exchange rate of 44 MK per US dollar from 25 MK per US dollar in June. The first devaluation was set at 34 MK per US dollar; then 3 days later, the announced rate was 44MK per US dollar. Furthermore, it was widely believed at the time that the central bank did not have enough foreign exchange to support the kwacha at that rate. In June 2000, the Malawian kwacha was trading at 54.81 MK per US dollar compared to 43.78 MK per US dollar in the fourth quarter of 1998 – a 25% increase. During the same period, the increase in the CPI was 49%.[5] This implies that the real value of the kwacha must have continued to appreciate since prices in Malawi rose at a much faster rate than did the nominal exchange and prices in the markets of Malawi's principal trading partners.

Although the high degree of volatility of the exchange rate created serious uncertainty for businesses and hampered the growth of trade, a more substantial depreciation of the local currency might not have boosted exports as much as one might expect. Malawi is a landlocked country with high transportation costs. Thus about 40 percent of the export bill comprises freight and insurance expenditures, and depreciation increases these costs. Furthermore, Malawi is an importer of fuel and is highly dependent on imported raw materials and intermediate inputs for industrial production and agricultural processing prior to export. In addition to the necessary capital investment and maintenance (spare parts), agricultural commodities require fertilizers and packaging materials. At the present time, fertilizer is wholly imported and the bulk of raw materials for producing packaging materials is also purchased from outside the country. Other exports, such as textiles, garments, yarns, processed chili, flowers, curios, pottery, pulses, ornamental fishes, and fresh vegetables, are heavily dependent on imported inputs. For instance, textiles require dyes; processed chili requires bottles, labels, and spices; and flowers require fertilizer and flower stocks. The costs of all of these are affected by changes in the exchange rate.

[5] International Monetary Fund, *International Financial Statistics*, December 2000.

There is no doubt that depreciation has been necessary. However, accompanying measures need to be put in place to ease the transition for firms. For instance, given that many firms import most of their raw materials and intermediate inputs, it is imperative to ensure that duty rates are as low as possible for these inputs. Where used in the production of goods that are subsequently exported, it is essential that there be an effective program for providing tax-free access to these inputs.

III. METHODOLOGY

A. Approach

The methodological approach used in this study was first developed by Associates for International Resources and Development (AIRD) to estimate the costs and benefits of eliminating institutional constraints on the expansion of nontraditional exports in Africa, with special emphasis on Ghana and Madagascar.[6] The approach was later extended to focus on the legal, regulatory, and judicial (LRJ) environment in Ghana, Madagascar, and Tanzania. Later, AIRD modified the approach with a study of the transaction costs associated with doing business in Cameroon.

The approach combines the practical insights of the business world with the more analytical perspective of economists. In a country with an industrial sector the size of Malawi, it involves a survey of approximately 30 private enterprises. The purpose of the survey is to assess the severity of the constraints facing different types of firms in order to identify the problems that should receive the highest priority. This assessment involves both the ranking of these constraints and the quantification of the costs imposed in terms of management time, tied up capital, and cash outlay. Statistical analysis is also used to examine the relationship between firm characteristics and the problems that managers consider to be most important.

Because of its nature, the study faced several challenges. First, firms are not used to thinking in terms of transaction costs. When questioned about their constraints, rare are those managers that identify all the costs that these constraints impose as an impediment to doing business. Second, justifiably or not, firms have grown tired and suspicious of enterprise surveys carried out to assess the private sector environment and to recommend reforms for policy change. Firms argue that they have never seen any substantive policy changes to their advantage.

The interviews with the firms, as well as the questionnaire, are designed to address these problems. The questionnaire comprises two parts. The first part seeks to gain a better understanding of the environment in which the firm operates from the manager's perspective. The firm is asked to identify the impediments to better use of its productive capacity. This enables the survey team and the managers to establish a good rapport and a broader perspective within which the detailed questions can be understood. During the second part of the interview, firms are asked to rank the constraints they initially identified and each is discussed in more detail. Managers are referred to the facts supplied during the first part of the meeting to provide the context for the information requested. Detailed questions concentrate on assessing the costs

[6] J. Dirck Stryker and Christopher Shaw, *Costs and Benefits of Eliminating Institutional Constraints on the Expansion of Nontraditional Exports*, Cambridge, MA: Associates for International Resources and Development, October 1994.

of personnel time, including that of the managers, the cost of tied-up capital, and cash outlays in addressing constraints already identified by the firm. The length of each questionnaire is such that an interview should not last more than one and one-half hours. Because of the need to gather information on key problems known best to upper management, interviews are scheduled whenever possible with Managing Directors.

1. Research Questions

This study seeks to answer the following key research questions, with some modifications depending on the revealed practical barriers faced by firms:

- What are the constraints facing firms with regard to: applying for a particular incentive regime; hiring, training, and discharging local and foreign workers; using procedures for tax-free access to inputs used in production destined for exportation; using and disposing of foreign exchange; financing post-shipment and pre-shipment activities; exporting and importing procedures; using or purchasing public utilities and services such as water, electricity, telecommunications, domestic transportation, and infrastructure when exporting regionally and overseas; knowledge and settlement of tax obligations; government agencies interfering with the daily activities of firms?

- Do these problems vary according to size, origin of ownership, quality and expertise of firm management, sector of activity, age of firm, level of success, and whether firms export overland or by sea or air? How can these problems be addressed in the short, medium, and long-term?

- How do firms perceive the government? Does the perception vary according to size or activity of the firm? Are government agencies more involved in the daily operations of firms? If so, which ones? What are the mandates of these agencies? How do they translate in the field? How can the relationship between firms and government be improved to promote business and encourage export growth?

2. Research Procedures

The research involved the following steps:

- Conduct preliminary interviews with government officials, business people, and representatives of the research community to gather information used to refine the draft questionnaire.

- Evaluate past studies and survey results to assess the extent to which some of the problems raised during these preliminary interviews have been studied before.

- Pre-test the draft survey instrument, using a few firms, in collaboration with Millennium Consulting Group, and revise questionnaire based on results of pre-test.

- Malawian Research Supervisory Committee participate actively in the selection of firms to be interviewed and in determining how the survey would be carried out.[7]

- Analysis of data collected and preparation of interim and final reports.

- Frequent consultation with Research Supervisory Committee to assure relevance and usefulness of survey results to policy.

B. Description of the sample

The survey was conducted on a purposeful selected sample of 30 firms primarily identified by the Research Supervisory Committee (RSC). Because of the nature of the survey, which required considerable cooperation on the part of senior management, it was not possible to choose the sample randomly. For firms to participate in this survey, they had to be medium or small enterprises (less than 50 employees) that were already exporting or had the potential to export. Attention was also paid to the need to maintain diversity of product, size, market orientation, and other characteristics.

The number of firms that actually responded was 20. Although this reduces to some extent the absolute size of the sample, the limited total number of small and medium industrial firms in Malawi implies that the sample is still relatively large compared with this total.[8] Furthermore, the limited resources available for the survey meant that it had to be exploratory rather than definitive with respect to its statistical reliability.

A significant number of the firms that responded to the survey were reluctant to provide information either because it was sensitive in nature or because they did not possess historical data on their performance and conduct of business. Another factor could be the great deal of suspicion that still exists concerning public institutions such as MIPA despite the commitment made in the highest spheres of government to support private sector activities.

Table 4 shows the age, ownership, capacity utilization, incentive regime, and market orientation for the interviewed firms. The sample includes the following industries: textile, food processing, packaging, beverages, agricultural inputs, metal fabrication, furniture, plastic products, fuels, and transport. Among the firms interviewed, 25 percent were exclusively producing for export markets (three of which were under export processing zone or “EPZ” status), of which 30 percent were exporting overseas while 60 percent were exporting regionally. Six out of the twenty firms were concentrating on the domestic market. The reasons for domestic market concentration varied from excess demand on the local market to lack of international market opportunities for ecologically specific products. On average, firms had low levels of capacity utilization irrespective of market orientation, capital /ownership, age and size -- for reasons explored in section C. Out of the 16 firms that supplied information on their capacity utilization, 10 had levels equal to or below 50 percent. Among the three firms operating at full capacity, two

[7] The Research Supervisory Committee was a committee made up of Malawian government officials, business leaders, and researchers for the purpose of overseeing the research and assuring its relevance for Malawian decision-making.
[8] Given the purposeful and non-random nature of sample selection, no effort was made to calculate the size of the sampling error.

were operating under EPZ status exporting clothing to South Africa and each was linked with a single customer. Because of lack of available data pertaining to employment, capital, or turnover, the team was not able to definitely classify firms by size. However, based on other sources the sample was principally comprised of medium size firms of about 20-50 employees.

IV. ANALYSIS OF CONSTRAINTS

A. Constraints Voiced by Firms

1. Results of unstructured interview

As mentioned earlier, the questionnaire was divided into two parts. During the first part of the interview, which was unstructured in nature, firms were asked to identify impediments to conducting business. As shown in Table 5, the recurrent themes were, by order of pervasiveness (number of firms mentioning the problem noted in parentheses): current state of utility services (17)); lack of security (6); high transport cost (6); small size of the local market (4); high cost of raw materials (4); competition from cheap imports (4); lack of skilled labor (4); lack of reliable supply of locally produced inputs (3); high taxes (2); high cost of finance (2); unpredictable government decisions (1); limited access to foreign exchange (1); and SGS inspections (1).

Table 4: Products of Sample Firms and Their Markets

Type of Product	Age of Firm Yrs	Ownership	Capacity Utilisation %	Incentive Regime**	Export Only	O.E.*	R.E*	Dom.*
Packaging Materials	30	Malawian	51	G (IRS)			X	X
Opaque Beer Brewery	1	Malawian	59	G				X
Maize Seed Breeder	4	Malawian	100	-				X
Packaging & Removals		Malawian	-	-		X	X	X
Rice Milling	5	British	50	G (IRS)			X	X
Confectioners	42	British	50	G (IRS)			X	X
Chillies and Hot Sauces	16	Malawian	80	G (IRS)		X	X	X
Dhall	10	Malawian	30	G (IRS)	X	X	X	
Dairy Products	2	Malawian	50	G (IRS)				X
Foundry	32	Malawian	-	B			X	X
Clothing	4	South	100	EPZ	X		X	
Plastic Products		Malawian	33	G (IRS)			X	X
Cut Flowers	14	Zimbabwea	50	EPZ	X	X		
Horticultural Products	2	Malawian	23	Special				X
Clothing	3	Malawian	100 Order	EPZ	X		X	
Mattresses & Foams	4	Malawian	33	G (IRS)				X
Furniture	21	British	Per Order	G (IRS)				X
Paprika & BEC	5	Dutch	30	G (IRS)	X	X		
Transport	13	Malawian	Per Order	Special			X	X
Ethanol	20	Malawian	75	B, G		X	X	X
Total					5	6	12	16
% of Total number of firms					25%	30%	60%	80%

Source: Firm survey
Notes:
*O.E. – Overseas Market; R.E – Regional Market; Dom. – Domestic Market
**B and G under incentive regime stand for companies that enjoy incentives for manufacturing under Bond and General Incentives respectively.
**IRS – Industrial Rebate Scheme

Table 5: List of Constraints as Identified by Firms in Unstructured Interview

irm Code	Type of Firm	Expensive Raw Material	High Transport Cost	Unpredictable Government Decisions	Small Domestic Market	Unreliable Utilities	Unreliable Supply of Local Inputs	High Taxes	Personal Safety	Competition from Cheap Imports	Lack of Skilled Labor	High Cost of Finance	Limited Access to Foreign Exchange	SGS
.01	Packaging Material Manufacturer	y	y	y	y	y								
.02	Opaque Beer Brewer	y	y			y	y	y	y					
.03	Maize Seed Breeder					y			y					
.04	Removals								y					
.05	Rice Milling						y		y					
.06	Confectioners	y	y		y	y				y	y	y		
.07	Chillies/Hot Sauces				y	y			y				y	y
.08	Dhall					y	y		y					
.09	Dairy Products		y			y								
.10	Foundry					y								
.11	Clothing					y								
.13	Plastic Products	y				y								
:01	Cut Flowers		y			y								
:02	Horticultural					y								
:03	Clothing					y								
:04	Mattresses					y		y						
:05	Furniture					y				y				
:06	Paprika & BEC					y								
:07	Transport									y				
;01	Ethanol		y		y	y				y				
	Totals	4	6	1	4	17	3	2	6	4	4	2	1	1

2. Results of structured interview focussed on capacity utilization

Once firms had identified within an unstructured framework the major constraints facing them, the interviewers probed further within a more structured interview format about the level of capacity utilization and the key problems constraining the use of that capacity. This format required the firms to prioritize the relative importance of each of these problems on a scale of 1 to 5, with 1= not a problem; 2= minor problem; 3= moderate problem; 4= problem; 5= major problem. The underlying assumption is that a striving private sector, required for sustainable growth in income and employment, will make efficient use of its capacity, if not expand it. A significant number of the firms interviewed were, for a variety of reasons, operating substantially below their installed capacity. Out of the 16 firms that supplied information on their level of capacity utilization, 10 had levels equal to or below 50 percent. Among the three firms operating at full capacity, two were operating under EPZ status and exporting clothing to South Africa to a single customer. The other firm sells exclusively on the domestic market but faces excess demand for its product.

Constraints to greater use of capacity are listed in Table 6 with the level of severity of each constraint denoted by the average score for the entire sample of firms. It is clear from this

Table 6: Ranking of Priority of Importance of Constraints

Constraint	Total Score	Average Score	Rank
Telephone	83	4.2	1
Electricity	71	3.6	2
Finance	66	3.3	3
Economic & Political	61	3.1	4
Water	53	2.7	5
Size of Domestic Market	51	2.6	6
Tax Regime	50	2.5	7
Qualified Labour	44	2.2	8
Supply of Imported Inputs	41	2.1	9
Suitable Premises	30	1.5	10

Source: Firm survey

table that costly and unreliable public utilities constitute the major problem constraining firms from making better use of existing capacity. Next in importance is the high cost and lack of access to working, and especially term, capital, followed by problems posed by the economic and political environment, such as lack of personal safety and macroeconomic instability. The limited size of the domestic market is also considered to be a significant problem, as are an oppressive tax regime, lack of qualified labor, and inadequate supply of imported inputs. These results broadly support those from the unstructured format.

B. Nature of Constraints

This section explores in some detail many of the constraints cited by the firms as constituting a significant problem or directly impeding higher utilization of their existing capacity. Other issues such as security and high transport costs are discussed later in the report.

1. Costly and unreliable public utilities

Costly and unreliable public utilities was by far the most critical obstacle cited by the firms interviewed. With regards to greater capacity use, the first concern was faulty communication lines, followed by unreliable power supply and poor water quality.

Telecommunication

In this new era of technological revolution, telecommunications is the core of the information infrastructure needed to participate and compete in the global economy. Lack of reliable telecommunication services is a severe impediment to conducting business. Yet, the telecommunications sector in Malawi still remains underdeveloped and faces a number of challenges. Telephone penetration is 0.31 per 100 of population compared to 0.5 for sub-Saharan Africa overall. It takes considerable time to be connected for a new service. Once the application is sent to Malawi Post and Telecommunication Corporation (MPTC), it can take up to three months before an agent is sent to survey the site and determine whether a line can be added. The application fee is MK1500.00 per line for an installation.

In addition to the time it takes to establish a new service, maintenance of existing connections is also dismal. It is not uncommon to wait up to six months before getting a phone line repaired. At times, although the lines are free, individual parties have difficulties establishing connections with the other party. The phone can ring indefinitely or the line is always busy. While it is difficult to assess costs associated with this problem, it is quite evident that this situation creates hardships for firms. Some of the problems experienced by the firms that were interviewed included:

- International communications difficulties
- Difficult to communicate with land lines
- Loss of export and domestic orders
- Delays in responding to orders
- Increased time and transport costs due to requirement of physical visits
- Loss of business with international customers
- Failure to get orders from customers and inputs from suppliers
- Increased transit time at border due to document or information in “transit”
- Bad impression to overseas customers

Because some firms contract up to 90% of their business via telephone and fax, many resort to the use of cellular phones to cope with these problems. Eighteen of the firms interviewed had to use cellular phones[9]. One limitation to such use is that the interconnection between cellular and regular phones managed by MPTC is not large enough. Thus it is very difficult to connect one network to the other. According to MPTC, the cost of the equipment including software is prohibitive. Also, the use of cellular phones is limited to a few cities. Until recently, only five cities had cellular phone capabilities: (Mzuzu, Zomba, Blantyre, Mangochi and Lilongwe). Finally, the use of cellular phones is quite expensive. The telephone situation leads many firms to buy cellular phones sooner than otherwise, yet firms report that operating costs of cell phones can be as much as 350 percent higher that of a regular phone, not including the price of the capital equipment.

The main problems of MPTC are insufficient capacity due to lack of cables, obsolete equipment, and vandalism of cable plant. There is a total capacity of 67,000 lines, but the existing cables (copper wires) only allow for 37,000 operating lines. One other issue is the quality of existing cables. Many were installed in the 1970s and the technology at the time did not allow proper insulation. During the rainy season especially, many lines are wet and create disruption. Among the three exchanges, the electromechanical exchange with the larger capacity creates the most problems. Parts for its equipment are no longer available, and little by little the equipment is loosing its redundancy leaving no backup support. In response to this problem, MPTC has installed a digital exchange to run in parallel with the electromechanical exchange. The digital exchange is much cheaper to run but still requires the use of cables. Malawi has attempted to go wireless without much success. The MPTC assessed that this technology is very expensive. It did not have the required technical expertise and ran into software problems. At the present time, MPTC is still assessing the wireless experience.

The MPTC is aware of the problems that the business community is facing and in order to address them has instituted plans to replace the old plant and equipment. A project is already underway which seeks to replace all old telecommunications equipment in the central region with 34,000 lines of digital equipment. Similarly, the old equipment in the Municipality of Zomba and its surrounding areas will be replaced by 6,000 lines of digital equipment under the same project. Funds have also been identified to finance another project for the replacement of old equipment in the Tea and Lower Shire areas. Meanwhile, a project is underway to rehabilitate the cable plant in Blantyre City and provide an additional 6,000 lines.

With regard to vandalism, the MPTC, with the co-operation of the police and the general public, has launched a campaign to patrol their equipment and plant and punish anybody caught in the act of vandalism. However, this has not solved the problem.

To further develop the telecommunication sector, the MPTC, in a joint venture with Telecom Malaysia, established a company known as Telecom Network Malawi (TNM) to operate a cellular phone service. However, the problem being faced by this service is congestion arising from the under dimensioning of the cellular network. The private sector is of the view that the

[9] One firm had a radio link and the other a satellite phone.

cellular phone service is expensive, though the MPTC indicates that costs may go down slightly in the future as the network expands and more customers take up services.

A major problem with the telecommunications sector is lack of competition. The MTPC is both the only operator and the regulator of the sector. A communications Sector Policy Statement was issued in August 1998 that aimed at liberalizing the sector, and the Communications Act of 1998 was passed in December 1998 to create a regulatory authority separate from MPTC to oversee this sector. This should facilitate the creation of an enabling environment for technology innovation and competition and thereby allow new entrants and operators into the telecommunication industry. Following the liberalization, newcomers have applied to offer cellular phone services; Celtel, for example, will be operational by the beginning of September 1999. Increased competition should lead to improvements in terms of efficiency and cost. In addition, operators need to be able to set prices in relation to the cost of service.

It is important that progress in liberalizing the telecommunications sector be carefully monitored. The current state of telecommunications has put Malawian firms at a disadvantage vis-à-vis their competitors. Malawian firms are deprived of an efficient use of the Internet to market themselves and gather trade and manufacturing intelligence. Increasingly, all aspects of business operations are being conducted electronically. Business to business relationships on the international scene rely increasingly on electronic communications.[10] While not sufficient, a cheap and reliable telecommunication infrastructure is necessary if Malawian firms wish to become competitive.

Electricity

Stable electricity is vital for promotion of the private sector and the economic development of Malawi in general. Experience has shown that as more countries are offering a relatively sound macroeconomic environment coupled with some measure of political stability, the overall quality of available infrastructure is a major determinant in attracting new investment, a stated objective of various public institutions such as MIPA and the Chamber of Commerce. Yet power generation and supply continue to be among the major problems facing industries in Malawi. Rates are costly and there are frequent unscheduled power interruptions due to increased demand and obsolete equipment. As shown in Table 7, firms report daily to monthly power outages that can last several hours at a time depending on the location.

Table 7: Monthly Outages

Number of monthly outages	1	2	3	5	6	8	10	15	20
Number of firms	2	1	1	1	1	1	2	3	5

Source: Firm survey

Currently, the Electricity Supply Commission of Malawi (ESCOM) has experienced delays in obtaining financing for major rehabilitation. As a result, ESCOM has suffered shortages of materials and equipment and has not been able to adequately carry out the rehabilitation

[10] "The Net Imperative: A Survey of Business and the Internet," *The Economist*, June 26-July 2, 1999.

required. Other reasons for poor electricity generation and supply by ESCOM include vandalism and poor work ethics among ESCOM employees.

To cope with power outages, firms usually protect their activities by purchasing alternate sources of power. Nine out of the twenty firms interviewed possess generators and their usage, capital cost, and operating cost for the first quarter of 1999 are shown in Table 8 below. Small and medium firms can resort to generators to maintain production, but the additional costs resulting from the purchase and operation of a generator weaken their often already precarious financial situation. Yet lack of a generator is even more devastating, as firms incur high costs with no returns. This is also the problem for larger and more capital-intensive firms, which cannot meet

Table 8: Power Failure Associated Costs

Capacity Generator	Capital cost (MK)	Annual Usage	Running Cost (MK)
500KVA	2.7 million	120 hrs	0.3 million
250KVA	1.8 million	1200 hrs	1.2 million
25 KVA	0.25 million	1400 hrs	.14 million
250 KVA	1.65 million	720 hrs	0.72 million
1.2 KVA	1.05 million	532 hrs	.004 million
2 x 180 KVA	2.16 million	840 hrs	.67 million
1.2 KVA	1.14 million	800 hrs	0.005 million
7.5 KVA (Office use)	.07 million	120 hrs	0.0035 million
660KVA	3.2 million	240 hrs	0.78 million

Source: Firm survey

their power needs from local generators. These firms suffer important production and capital losses, which act as a major impediment to their profitability.

In addition to the extra investment in power generators, three of the interviewed firms reported having to carry higher inventories of finished products so as to supply their customers during power outages. One firm also had acquired an all risks insurance policy (annual premium MK10,000.00) primarily to cover damage due to power surges. For another company (rice milling), the capacity on their equipment was simply too large to be run by a standby generator.

Until recently, ESCOM has had a monopoly on both the generation and distribution of electrical power. Yet it has been unable to come up with the financing required to rehabilitate its equipment and provide reliable electrical power service. Legislation has been recently passed to liberalize the distribution of power. The same should be done for its generation. This will enable private operators to invest in alternative sources of energy. In order to maintain fairness in competition, it is essential to set up a regulatory body to oversee the energy sector.

Furthermore, all parties involved in power generation or distribution should be able to determine their own prices to reflect their individual cost structures. ESCOM employees should also be trained to properly maintain the equipment and improve the quality of service delivered.

It is important to note that Malawi is not currently connected to the Southern Africa Power Pool (SAPP) power sharing grid. Recent research under the Trade Regimes and Growth component of the EAGER project has shown that there are enormous potential gains for countries in Southern Africa to share their electrical power.[11] This is particularly true for Malawi, which could benefit enormously, for example, from low cost power available at the Cabora Bassa dam in Mozambique. Issues that need exploring include the extent to which Malawi is willing to be dependent on external sources of power, how power distribution from this source can best be organized, how this distribution should be linked with the distribution of locally generated power, what Malawi should pay for this electricity, and what the rate structure should be to Malawi's users.

Water

Urban water supplies are inadequate for industries that require vast amounts of water. Similar to electricity, water supplies tend to be unreliable as well. Until recently, water was provided by a government department, except in Blantyre and Lilongwe. Now, all provision of water is in the hands of regional boards, which are expected to improve delivery. Although not as severe a constraint as the other utilities, water is still imposing a cost to the firms as is shown in Table 9.

Table 9: Water Coping Mechanisms and Related Issues

Coping Mechanism	Firms Affected	Problems Resulting from Water Disruptions
Water tanks/pumps	8	Production stoppage Inconsistent water treatment detrimental to production High loss of plants due to withering Hygiene problems Close operations
Boreholes	2	
Shallow wells	1	
Dams	1	
Rivers	1	

Source: Firm survey

2. Lack of access to and high cost of finance

Malawi has a relatively limited financial system consisting of a central bank, five commercial banks, four development finance institutions, two savings institutions, three leasing companies, one finance company, a building society, several insurance companies, and a number of pension funds. The Reserve Bank of Malawi (RBM) is responsible for ensuring monetary stability, maintaining a sound financial system, managing foreign exchange, serving as lender of last resort to the banking system, and acting as advisor to the government on monetary affairs. The

[11] F.T. Sparrow and William A. Masters," Modeling Electricity Trade in Southern Africa – 1999", Purdue University, November 1998

RBM regulates and supervises the activities of banks and financial institutions, and is responsible for the processing of their applications for licenses and registration.

Financial regulation covers a number of regulatory measures designed to achieve diverse objectives, which may be classified into six broad categories:

- Macroeconomic controls are focused on maintaining control over overall economic activity; they consist mainly of mandatory reserve requirements and regulations over interest rates and foreign investments and transactions.
- Selective credit programs, mandatory investments in certain sectors, and preferential rates of interest constitute the main instruments for controlling and influencing the overall allocation of resources.
- To control and influence the structure of the economy, the principal regulatory measures cover entry and mergers, geographic coverage, and limits on the range of activities and services of different types of financial institutions.
- Prudential controls preserve the safety and soundness of institutions in the financial system through minimum capital adequacy standards, limits on concentration of risk, reporting and surveillance requirements, and portfolio classification and provision standards.
- Organizational controls are intended to facilitate the efficient functioning and integrity of financial markets and the exchange of information through measures over disclosure of market information, setting of minimum technical standards, and rules for market making and participation.
- To provide protection to users of financial products and services, the main regulatory measures cover disclosure of information to customers and the public, interest rate ceilings, and compensatory deposit insurance mechanisms.

Malawi's financial situation has experienced severe disruptions in the recent past. In early 1994, increasing problems of expenditure control became evident in advance of the first multiparty elections, and administrative problems in revenue collection led to a large overall fiscal deficit mainly financed by the banking sector. Strong upward pressure on food prices induced by a severe drought and devaluation further fueled inflation. This led to the inception of programs to re-establish financial stability and to set the basis for sustainable growth. Over the period 1994-95-1996/97, the Government of Malawi reduced its overall budget deficit (excluding grants) by 20 percentage points of GDP, as a result of significant measures to curtail expenditure and to improve the administration and collection of taxes. The fiscal adjustment allowed the adoption of a tight monetary policy, which helped to decrease the inflation rate to less than 7 percent in 1996.[12] However, inflation thereafter increased from a little less than 10 percent in 1997 to 29.8 percent in 1998.

High rates of inflation have impacted negatively on the private sector in several ways: first, firms encounter escalating and uncertain input costs, especially those of raw materials, intermediate products, capital goods, and labor. Second, a tight money policy to control inflation results in conservative lending policy with a tendency to lend short-term rather than medium or long-term, thus encouraging trading activities at the expense of manufacturing. Third, individuals' real

[12] IMF, Malawi Recent Economic Development, 1997

incomes fall as wages and salaries are not adjusted in line with inflation. Finally, the need to cover government fiscal deficits tends to crowd the private sector out of capital markets.

In order to finance its deficit, the government is in active competition with the rest of the economy for available credit. For example, the rate offered in 1999 on treasury bills was 45%-48% p.a. yield, compared to the 33%-40% p.a. interest rates on savings and fixed deposits offered by banks and finance companies. The base lending rates of banks and finance companies ranged between 42% and 52% p.a. The liquidity reserve requirement on deposits was also fairly high at 35%, and even though a 14.29% p.a. interest was paid by the Reserve Bank of Malawi (RBM) on these liquidity reserve deposits, the cost to banks and other financial institutions of holding these reserves was obviously very high.

Given the current state of affairs, it is no surprise that lack of finance and its high cost are a major problem to firms. Even though real rates of interest may not be terribly high, given the rate of inflation, firms are still understandably reluctant to borrow at 42% to 52% no matter what the rate of inflation. Recourse to the financial system is therefore minimal, because of high nominal interest rates, and the majority of firms interviewed were financing their working and long-term capital needs through internally generated funds.

It is important to underscore that other factors can also preclude firms from accessing finance through banks and other institutions. It may be that these firms are engaged in unprofitable ventures that no bankers or investors would want to finance. It may also be that firms lack the culture of supplying transparent financial statements necessary to properly evaluate a loan or investment decision. Nevertheless, the effects of such high rates of interest and of such variable rates of inflation, as are shown in Table 10, are devastating to the liquidity needs of the private sector. This was evidenced by the high priority attached by firms to lack of stability in the macroeconomic environment.

The high cost of finance is also a result of a lack of competition among financial institutions. Most of the established institutions in the financial sector in Malawi are tied directly or indirectly to Government or state-owned enterprises. As a result, the financial sector is highly concentrated, resulting in high margins and lack of competition in the range of services and financial instruments offered. Banks and development finance institutions exhibit a preference for lending to larger and more established institutions. In recent years, there has been an evolution of credit schemes tailored to small and micro enterprises, but these charge concessional rates of interest that have distorted the market. Although these institutions have brought relief to some profitable businesses, many have encouraged business ventures that would not be sustainable if commercial rates of interest were charged.

Sampled firms complained about the complexity of procedures and collateral or equity requirement from banks. Formal financial institutions require that the borrower pledges tangible immovable assets, such as land, as security for the loan. These are assets which most small and medium enterprises (SME's), by their very nature, do not have. If they have land, it might not be secured through formal ownership title. As a result, banks will not accept such land as security. Equity contribution ranges from 20 to 35 percent of total project or loan requirement. Even though this is relatively low in comparison with other African countries, it is not an easy requirement for SME's to fulfill. Thus there is a need to develop specialized financial institutions that would cater to small and medium firms' needs in ways that are financially sustainable.

Table 10: Interest rates

	1991	1992	1993	1994	1995	1996	1997
Reserve Bank rate	14	20	25	40	50	27	32.5
91-day Treasury bills	11.5	16.5	22.3	45.6	53.3	13.9	30.92
Commercial bank prime rate	14	21	26	40	48	26	43
Savings Deposits	13	17	22	23	33	12.5	26
Minimum mortgage rate	12.75	12.75	19.75	19.75	34	30	33
Leasing & Financing	25	31	36	36	56	36.50	49
3-month time deposits	13.5	19.75	24.75	24.75	44.75	11.50	25
12-month time deposits	na	21.25	26.25	26.25	40		26.5
Local registered stock		15.5	23.75	38	38	38	
Consumer price inflation	12.5	36.1	18.3	66	75	6.70	9.6
Real interest rates							
Commercial banks							
Prime lending rates	1.5	-11.10	6.5	-15.70	-16.10	18.10	
Savings deposits		-11.80	4.8	-19.30	-24	5.9	
12-month time deposits		-12.00	5.5	-19.90		3.10	
Local registered stock		-15.10	4.60	-16.90	-21.10	29.30	

Source: IMF, Malawi Recent Economic Development, 1997.

Finally, despite a relatively well-established stock exchange, none of the firms interviewed have considered going public in order to raise much needed funds for medium and long-term investments. This has been partly because most businesses are family owned. Thus, there is a natural reluctance to lose control of a family business. Furthermore, it is not clear that firms have the internal capacity or the desire to fulfil the financial and accounting reporting requirements in order to be listed on the stock exchange.

3. Uncertain economic environment

The relatively unstable macroeconomic environment of Malawi has had a negative influence on private sector development. High rates of inflation and unstable exchange rates have meant that returns on private sector activities are uncertain, and this has impeded utilization of existing capacity and new investment.

Perhaps the major barrier to economic growth in Malawi is the existence of a persistently overvalued and unstable real exchange rate. This biases the allocation of resources away from the export sector, because of low export prices measured in terms of local currency, and it encourages measures to protect against imports, which in turn further distorts resources and encourages rent-seeking behavior. It also results in enormous uncertainty for producers and investors.

Since partial liberalization of financial markets in 1994, Malawi has been unable to sustain a stable real effective exchange rate. Corrective nominal devaluation at times has given way to periods of appreciation of the real exchange rate due to domestic inflation that was higher than that of trading partners. Unpredictable real exchange rates have placed pressures on exporters and importers. Such changes create an exchange risk for companies, which stand to lose if there is devaluation between the time that they set their domestic selling prices, and the date the Malawi kwacha realized from their sales is converted into foreign exchange. There is also considerable uncertainty regarding the prices that they will have to pay for imported inputs.

As an example, the real effective exchange rate based on purchasing power parity (PPP) in Malawi remained highly overvalued until early 1994, when there was a substantial depreciation of the nominal rate. By 1997, however, the real rate had appreciated almost back to its level before 1994 because of the effort to peg the kwacha to the dollar in the face of strong inflationary pressure. Subsequently, there was further depreciation in the real rate associated with the abrupt devaluation of August 1998. But by June 2000, the real rate had appreciated substantially once more. According to the World Bank, a 1.0 percent appreciation of the real exchange rate leads to a decrease in non-traditional export growth of 1.5 percent. In other words, overvaluation has more than offset the benefits of tax incentives on raw materials, intermediate products, and capital goods used in production.

In order to control access to scarce foreign exchange, the government limits retention of foreign exchange by exporters to 30-35 percent of their earnings. Although only one exporting firm reported experiencing delays in acquiring foreign exchange, there is some evidence to suggest that restrictions on and delays in processing bank loan applications is a way of allocating scarce foreign exchange. Our survey indicated that inadequate finance was one of the most severe constraints on increasing utilization of existing capacity and on expanding that capacity. Although restricted access to foreign exchange was not the only reason for unavailability of finance, it certainly contributed. Furthermore, the degree of overvaluation has been such that there must have been other ways of controlling access to foreign exchange – ways that do not appear to be very well understood. These have caused severe disruptions in the market for foreign exchange and further uncertainty on the part of producers and investors.

This unstable macroeconomic environment affects the whole economy. The majority of sampled firms, especially those selling on the domestic market, complained about sharp devaluations and lack of trust because of inconsistencies in government exchange rate policies. To cover these risks, firms seek to include a premium in their selling prices based on their expectation of the exchange rate at the time that their sales realizations are converted into hard currency. This premium represents a real cost to business.

Management of its exchange rate is not an easy task and requires careful analysis, especially because Malawi has an economy highly dependant on climatic conditions, with underdeveloped financial markets and a narrow export base. If the exchange rate is allowed to float, external disturbances can have a profound impact on the exchange rate, and on the profitability of exports, especially nontraditional exports that normally have relatively low profit margins. If the central bank tries to mitigate these effects through the buying and selling of foreign exchange, it runs the risk of losing reserves and the confidence of the public, resulting in speculative pressures being added to external forces. Fiscal instability only adds to these pressures.

4. Inadequate physical security

The deterioration in physical security is also of major concern to firms. Since the era of multiparty democracy, initiated in 1994, Malawi has seen an escalation in crime of all sorts. Business has been adversely affected by fraud and forgery, but more seriously by robbery, especially armed robbery which has often resulted in loss of lives and property.

All firms doing business in rural areas have deplored the high incidence of theft during the buying season. As a result, some services in rural areas, including banking and distribution of goods, are being withdrawn due to security concerns. Travel and transportation at night have become risky, further restricting delivery of goods and services to rural areas.

Urban centers are not immune to this plague and some firms have reportedly made significant investments to secure and fortify their factories and warehouses. One foreign investor was reported to have declined to increase his investment in an otherwise profitable entity because of concerns about the economic climate and deteriorating security.

Various arguments have been put forth to explain the current state of affairs. Some argue that multiparty democracy has been misconstrued to mean freedom to do whatever one likes, while the end of civil war in Mozambique has made small firearms readily available. Others contend that the government's inability to deal with the political transition is a factor. The abolition of the youth movement that supported the small police force has created a vacuum. Then there is the legal requirement that a suspect should be charged within 48 hours of committing a crime. The courts have limited capacity to handle cases and this leads to freeing of some criminals from police custody, leaving many crimes unpunished. Finally, there is the hypothesis that poverty and high unemployment rates are conducive to crime. It's very likely that all above-mentioned factors play a role in the rising level of criminality in Malawi.

All of this has a detrimental effect on many industries, including tourism, and can create a perception of high risk among potential investors. To tackle the problem, the government has increased the size of the police force, the number of vehicles for patrolling, and other facilities. However, these changes have been marginal and have not significantly improved the security situation. There is need to accord top priority to improving security by allocating more resources to the police and the judiciary, and by easing economic hardships.

5. Weak domestic market

A number of firms, especially those selling exclusively on the domestic market, complained about weak domestic demand for their goods due to competition from imports and lack of income growth. Following years of import substitution, firms have grown accustomed to operating behind protective barriers and lack the skills to successfully compete in a more liberalized economy. This is further exacerbated by the monopolistic nature of the Malawian economy, which precludes small and medium firms from growing and capturing additional market shares.

Only about 15-20 percent of total output is produced by the private sector. The private sector in Malawi is made up of a large number of micro enterprises, a small number of small and medium enterprises, and a few large firms. This structure obviously implies structural weakness in the development of the private sector. Table 11 gives comparative data on the enterprise structure in Malawi, Ethiopia, and Botswana.

Table 11: Enterprise Structure of Malawi, Ethiopia, and Botswana

	Malawi	**Ethiopia**	**Botswana**
Large	0.04%	0.07%	4.2%
Small & Medium	3.6%	3.8%	50.1%
Micro	96.36%	96.13%	45.7%

Source: CTA Private Sector Development Study, Ministry of Commerce and Industry

Most industries in Malawi are characterized by an oligopolistic or monopolistic market structure, with a few key players dominating the market. Examples include sugar, petroleum fuels, soaps, cement and beverages. In addition to high market concentration, a number of firms also have vertical and horizontal interests through interlocking directorates, e.g., Press Corporation Limited (PCL) has significant shares in National Bank and Commercial Bank.

The vast majority of SMEs sell their products directly to the final consumer, rather than to medium or large enterprises. On the other hand, the larger firms import most of their inputs. There is little evidence of sub-contracting between SMEs and larger organizations. In most cases, it is said that SMEs produce products of low and inconsistent quality standards. SMEs are also said not to be able to honor pre-agreed schedules of product delivery, routinely falling behind schedule.

It is generally accepted that the number of support and ancillary industries, composed primarily of small and medium-scale enterprises, required to service the main sectors of an economy multiplies with diversification and degree of value added. Malawi’s narrow commodity base and low level of value added has had a constraining effect on the development of such industries. This narrow commodity base is a result of the previous strategy of concentrating on agriculture, especially the traditional crops of tobacco, tea, and sugar. For example, in the 1970’s and 1980’s, there was a deliberate policy by commercial banks to provide preferential credit terms to the tobacco industry. As Malawi’s economy diversifies through greater processing and development of nontraditional exports, it will be important to maximize the linkages of these firms with other sectors of the economy.

An important question is whether growth in Malawi is likely to occur from the expansion of larger firms, with benefits spreading more broadly through their hiring and through their linkages with other, smaller firms, or whether it will occur because smaller firms grow to be larger firms. At present, Malawi’s government appears to believe that there is a need for greater opportunities for smaller firms. In an attempt to foster local competition, the government has finalized a Competition Law and Policy to address restrictive business practices. The Competition Act, which was recently passed by Parliament, aims to curtail restrictive business practices through (a) removing barriers to entry (b) making restrictive business practices offences, and (c) protecting the consumer. The thrust of this effort appears to be an attempt to open domestic markets to a wider number of firms.

Although greater competition is certainly to be encouraged, there is reason to suspect that most employment will not be generated by the expansion of smaller firms. The Regional Program in Enterprise Development (RPED) studies, being funded in a number of African countries by the World Bank, suggest that growth of employment occurs mostly through the expansion of larger firms and their linkages with supplying and service industries, which are more likely to be made up of small and medium enterprises.[13] Thus lack of these linkages can be very detrimental to growth with equity.

6. Disincentives created by the tax regime

By 1995, the Government of Malawi had put in place tax policy reforms needed to encourage the growth and diversification of nontraditional exports, which had been stagnant despite a cheap labor force that could make Malawi competitive for export production and attract export-oriented foreign investment in labor-intensive sectors. A number of tax reform measures were instituted that sought to reduce the anti-export bias resulting from high degrees of protection for import-competing industries created through high customs duties. Particular attention was paid to inputs used in the production of exports. Given the fact that exporters must compete actively on world markets with producers from other countries, it was imperative that their costs be kept to a minimum. This implies that they needed to be able to use intermediate inputs that are not taxed and, if imported, come into the country with a minimum of expense and delay.

Tax incentives in Malawi pertain to concessions with respect to indirect and/or direct taxes. Several arrangements are in effect, some of which relate specifically to indirect taxes (customs duties, excise taxes, and surtax - a variant of the value added tax). One relates to direct taxes, and there are export processing zone (EPZ)/bonded warehouse arrangements that involve concessions of both types.

Industrial Rebate Scheme

The Industrial Rebate Scheme is a duty exemption scheme such that registered manufacturers can import approved inputs – raw materials and intermediate goods - duty free. The scheme is designed to aid domestic manufacturers, whether producing for the local market or for export. It is not specifically an export tax incentive. Furthermore, this relief does not apply to surtaxes or any excise taxes that may be payable on either imported or domestically produced inputs.

[13] Tyler Biggs and Pradeep Srivastava, *Structural Aspects of Manufacturing in Sub-Saharan Africa; Findings from a Seven Country Enterprise Survey,* World Bank Discussion Paper No. 346, World Bank, 1996, pp. 40-49.

Ten of the firms interviewed qualified under this scheme. Only six were taking full advantage of the scheme while four did not fully enjoy the benefits due to the fact that some of their raw materials were not on the approved list. The raw materials that were not on the approved list were ones that can be found locally and are sourced from outside because of price, quality differential, or availability owing to seasonality of supply or climatic conditions. (e.g. agriculture-based raw materials).

Only manufacturers registered to pay surtax are eligible for rebates. A small-scale manufacturer not meeting the threshold for surtax registration can nonetheless register voluntarily in order to be eligible for rebates. Most small exporters are excluded from the scheme. These are mostly in the horticulture industry, exporting agricultural produce to European markets on a very small scale. Although they have formed an association to meet the production level requirement, Customs has resisted registering the association, arguing that growing produce is not manufacturing. Consequently, these small exporters are at a disadvantage vis-à-vis their competition overseas since they pay duties on inputs used in the production of exports. This argument is not applied, however, to the cut flower industry, which benefits from zero duty rates on designated inputs.

For a qualified firm to register, it has to go through a lengthy process with no sure outcome. The registration starts with an application at the Customs head office. Once the application is verified, it is submitted to Treasury. The latter approves the application and forwards it to the Ministry of Justice, which prepares a government gazette notice for signature by the Minister of Finance. Once the Minister of Finance has signed the gazette notice, the notice is sent back to the Ministry of Justice for publication. The gazette notice provides total duty relief for designated inputs applicable to an industry, which is extended to other firms upon application to the Controller of Customs. This process lasts at least 3 months, but there is no guarantee beyond that. There is no doubt that firms would greatly benefit from a more streamlined and certain system.

It is not uncommon to see imported inputs for manufacturers diverted to the local market. If a firm is proven guilty, it faces stiff penalties and the requirement to enter into bond with sufficient surety to cover the duty rebated. Computerized reporting would enable Customs Officers to adequately check claims made by various importers, as export reporting would be cross-checked with importation documents.

Duty Drawback Scheme

This concession, authorised by the Export Incentives Act, involves a refund of duty paid (import duties, surtax, and excise taxes) on imported goods and materials incorporated into products that are subsequently exported. Unlike the industrial rebate which works for an entire industry, the Duty Drawback Scheme operates on a case by case basis requiring firms to submit applications based on detailed, auditable evidence that duty and taxes were actually paid, inputs were actually used, and exports actually took place.

In order to qualify, a producer must register with the Malawi Export Promotion Council (MEPC), and is supposed to renew its registration annually on the basis of a return giving turnover, exports, use of credit, and description of problems encountered. If it finds the application legitimate, MEPC issues a certificate of registration, which is copied to five government agencies. This serves as a basis for Customs and Excise to refund duty on inputs incorporated in exported goods and for the Commissioner of Taxes to accord a twelve percent tax allowance.

The Controller of Customs and Excise is mandated by the Customs and Excise Act to effect a duty drawback immediately and at a place where products are exported upon proof that the goods relating to the claim have been exported and that the duty and other taxes had originally been paid. Goods subject to duty drawback are entered on a Form 34A. A copy of the Form is shipped with the goods to the port of exit where a customs officer certifies exportation of goods. Duty drawback is paid only when certificate of exportation is completed and two other Forms (44A and 44B) have been filled in. Seven copies of each are required. Once the request has been approved, 75 percent of the claim is authorized for payment. The remaining 25 percent is to be paid within 60 days of verification of claimant's commercial records.

Although some were qualified, none of the firms in the sample had used this scheme because they viewed it as cumbersome. They complained about the number of forms to fill out, and the time it takes to be fully reimbursed. It is not unusual that there are no funds to make a payment even after a claim is verified eligible for payment. The problem has been exacerbated by the introduction of the Cash Budget System where the Department of Customs reports gross revenues to Treasury. The Customs law does not provide for interest payment for delays in refund by Government. Thus the value of the drawback is eroded by inflation, financial charges, and administrative costs. Delays in payment have at times been up to 9 months. In addition, many applications are denied on technicalities. As a result, very little use is made of this scheme even though many firms reported not being able to afford duties in addition to the cost of spare parts and capital equipment

The drawback system used in Malawi only takes applications from exporters who have directly imported the dutiable inputs. This induces vertical integration and denies duty-free rights to domestic suppliers of the inputs used in exported goods. The drawback system could only apply to the domestic suppliers if there was a clear indication that the locally furnished inputs were only used in the production of exports. Due to the complications in applying the duty drawback system to domestic suppliers, some countries get around this problem by allowing duty relief to be calculated on the basis of sets of input-output coefficients for a limited number of frequently exported goods. The actual amount of the drawback could be estimated based on these coefficients whose rates would be published and periodically revised. This is not done in Malawi.

Surtax Scheme

In the past three years the Government of Malawi has been implementing a medium term tariff policy and surtax reform plan with the objective of reducing distortions in the tariff system, and transferring the burden of revenue collections to the surtax. Because the surtax system operates along the principles of a value added tax (VAT) and the system is destination based, exports are supposed to be zero-rated; that is, all surtaxes paid on inputs for merchandise that is exported should be refunded.

The surtax system does not operate effectively or fairly, at least concerning reimbursements for taxes paid on inputs used in the production of exports. Government's failure to reimburse tax credit has eroded confidence in the surtax system and may encourage non-compliance and evasion.

Need for simplified tax exemption system

It is evident that the various schemes for granting exemption on indirect taxes paid on inputs used in the production of exports work very imperfectly. The rationale behind the Industrial Rebate Scheme is unclear. It does not offer an incentive to export. The scheme also favors larger over smaller producers. The Duty Drawback and Surtax Schemes are appropriate in their incentive structures but do not work well administratively. The only scheme that does work reasonably well is the Export Processing Zone/Bonded Warehouse Scheme, but this is clearly biased against smaller firms. None of the schemes effectively allows for exemption on taxes paid on inputs that are produced locally but are subsequently incorporated into products that are exported.

What is needed, as noted above, is a program that estimates the tax content of exports based on a set of coefficients and provides either immediate payment for these taxes or offers a negotiable credit against payment of other taxes. Immediate payment will require some sort of revolving fund. Experience with these is not very good since the funds tend to become depleted. A better option is a negotiable tax credit, which can either be used by the exporter in lieu of other tax payments or sold on the open market.

7. Labor Market

Given the poor state of Malawi's educational standards, which puts people at a disadvantage for employment in industry or agriculture,[14] it's not surprising that 9 firms (a little less than 50%) considered lack of qualified labor as a major obstacle to the development of their businesses. This ratio is important if we consider that many of the firms included in the sample were low-skill, labor-intensive operations. For some firms, the issue of lack of qualified labor for unskilled or low-skilled employment was of importance. For others it was the issue of a lack of highly skilled local people, requiring them to seek foreign expertise.

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[14] Adult illiteracy in Malawi is high, at 44% of the population, while in neighboring Tanzania, which is considerably poorer, only 32 % of the population is illiterate. Very few, around 4.5 % of those Malawian students who attend primary school, carry on to secondary education. Poorer neighboring countries such a Mozambique and Tanzania achieve better results, at 7.5% and 5.5 % respectively. In Africa, Malawi's public primary schools are among the most destitute. According to statistics from the education ministry, in 1992/1993 it was estimated that there were 78 children per qualified teacher, 18 students per desk, 32 children per chair and 102 students per classroom. Malawi's poor educational standards not only make people ill-suited for manufacturing employment, but also put them at a disadvantage for agriculture. Surveys have found that the little-educated rural poor are not well-equipped to grow crops needing intensive care such as tobacco.

Unskilled or low skilled labor

The issue of lack of trained labor is very important as it affects many firms and institutions. Firms reported that unskilled workers usually lack rudimentary literacy and numeracy skills. This precludes them from accessing better paid jobs or performing more efficiently on their existing jobs. For instance, workers that can hardly read or count cannot fill an order, read labels, or respond to written requests. While firms recognize the problem, it is not up to them to provide elementary schooling to their workers. Interestingly, none of the firms sampled have been creative enough in trying to address this issue. For instance, one could think of using color coded materials to communicate with workers who have not mastered English.

Skilled labor

The scarcity of skilled labor for mid and upper managerial positions is also an issue. The problem is so acute that once a good employee is well trained, it is very likely that he or she will seek employment that pays better. For instance, a trained freight forwarding agent can easily find a high paying job with a large company, which does its own clearing and forwarding. It appears as though firms that pay above market wages (15% and above) have less of a problem of retaining trained labor. Firms that cannot afford very high wages lose a lot of their trained labor. Similarly, firms have reported keeping unqualified workers on their payroll because of lack of proper replacements.

The issue is what type of training should be provided and who will finance training programs. A suggestion is first to foster primary education. Second, Malawi should have technical vocational training institutes established in partnership with the private sector. This would ensure that people would receive formal training geared towards private sector needs. The curriculum would be developed in partnership with firms. At the end of the training, students should participate in job fairs where they would be able to sell their skills. The programs should be geared towards adults and should be community based. The curriculum could be developed in partnership with the different chapters of the Southern Africa Enterprise Network, a network of private business leaders in a number of Southern African countries. While its conceptual framework is appealing to private and public managers, the financial aspect of such programs is open for debate. Who will finance? How much should each firm contribute? Who will manage the institute and its finances?

Recent experience elsewhere in Southern Africa emphasizes the importance of intimate involvement of the private sector in industrial training. In Botswana, for example, "industry-wide training schemes were established and each company required to provide a lecturer and course terms of reference. Only when successful candidates passed examinations was a percentage of the employee's salary reimbursed to the respective company."[15] Botswana has successfully made the transition from an economy based essentially on diamonds to one in which labor-intensive, export-oriented industry is of considerable importance. This shows that the task

[15] USAID/Mali Africa Trade and Investment Training Program, "Textile Sector Prospects and Strategic Planning", draft, July 22, 1999, p. 14.

is not impossible but will require a high level of cooperation between the private sector and government.

The Employers' Consultative Association of Malawi (ECAM) and the Malawi Congress Trade Union (MCTU) should have key roles to play in the setting up of such training facilities. At the present time, and not surprisingly, both institutions are at odds. ECAM argues that MCTU is mainly concerned with wage increases while discounting the issue of labor productivity. While MCTU complains about an underpaid labor force, most ECAM members try to assure proper remuneration. As an example, a recent study conducted by ECAM showed that the minimum wage of 21.90 MK per day set by the Ministry of Labor following devaluation in 1998 was lower than the living minimum wage of 36 MK per day determined by ECAM, and usually surpassed by its members. ECAM contends that MCTU should expand its role and discuss the notion of productivity with its members. MCTU argues that employers do not consider employees as resources and are reluctant to properly train them or pay them adequate wages.

Foreign expertise

Firms that viewed the lack of skilled labor as a key obstacle had a strong urge to engage expatriate personnel. However, they were frustrated with lengthy and bureaucratic delays in the issuance of Temporary Employment Permits (TEP). All the ten firms using foreign expertise reported delays varying between 3 and 10 months. These delays concern new permits and renewals. Delays related to assuring the legitimacy of TEP requests act as a disincentive to investors.

A new policy has been proposed to revise the issuance of TEPs in order to remove the barriers as perceived by firms. In the past, the number of TEPs was pegged to the level of investment, and the firm had to be export oriented. This biased the process against small initial investors. Also, each TEP was subject to scrutiny by all ministries involved in the approval process. This created unnecessary delays and arbitrary refusals. The revised policy proposes automatic issuance of employment permits for up to four key personnel depending on the level of investment. Also, all ministries would gather in one clearing-house in the form of a committee and would make a recommendation to the Ministry of Home Affairs, which would grant approvals.

The proposed policy allows a firm to get employment permits for two types of expatriate personnel: key posts and time posts. Key-post positions allow firms to have expatriates on staff for the length of the project. For time-post positions, the policy provides for 3-year TEPs for personnel in short supply in Malawi. The permit can be renewed once – and thus can last 6 years. After this period, the firm has to find someone to replace the expatriate on the time-post. This implies that the firm has to have a training program that would allow it to have a pool of qualified candidates from which to choose the replacement for the post. In the past, the firm had to groom one specific person who would replace the expatriate. It is now up to the firm to create a pool of qualified candidates to choose from.

Now that the policy has been revised, the next question is implementation. The new system will work as follows: A firm will submit an application to Immigration, which will in turn forward the application to the Secretariat Committee (held within the Ministry of Labor). The Secretariat includes Home Affairs (which drafted the policy), Immigration (for implementation), the Ministry of Commerce and Industry, and MIPA. The secretariat will make a recommendation to the Ministry of Home Affairs, which will make the final decision. The Minister of Home Affairs has to affix his or her signature on the approved documents. If a decision is to be contested, the appeal has to be filed with the Ministry of Home Affairs. The entire process should take less than 40 days. However, there is no clause that would grant automatic approval if nothing happens within the 40 days following the submission of the application. Furthermore, it is believed that the personnel in charge of implementing the policy are not well trained. In the past, institutions involved in the issuance of employment permits were also policing and curtailing illegal immigration.

In the new system, one key issue is to have adequate training programs within the firm. The training program is subject to review by the Ministry of Labor. Given the lack of qualified labor, such training programs are likely to be expensive. Again, an emphasis on the replacement of expatriate labor by local employees should be accompanied by measures showing the commitment of public agencies to provide trained labor. The burden of training workers should not only be borne by firms but also should be shared between public and private agencies.
On paper, the new TEP policy is generally considered to be a move in the right direction. However, implementation is still riddled with bureaucracy (and by individuals unfamiliar with business), takes too long, and is subject to abuse. This constraint mostly affects enterprises in the manufacturing sector, especially exporters, importers, foreign investors, and new entrants. In October, a South African firm with a request for TEPs placed in June had not yet received a response. Similarly, some of the surveyed firms argue that the new policy has not yet been implemented, as they requested renewal of some of their TEPs several months earlier.

If Malawi wants to achieve rapid export growth, one prerequisite is to attract foreign investment and expertise. Foreign exporters typically play an important role in catalyzing the take-off of exports in low-income countries. Besides ready accessibility to finance, they possess the know-how as well as information on international trends, marketing connections, and technology. Malawi should drastically streamline implementation procedures for TEPs. While it's true that one or two jobs might have been taken away from qualified Malawians, the foreign expertise will lead to many more jobs.

Labor productivity

Low labor productivity was raised as a problem by sampled firms in a few instances. However, firms were not able to substantiate their claim by providing benchmarks from domestic competitors or similar firms in other countries. This is not to say that their claims are unfounded.

The poor general state of health contributes to a largely unproductive workforce. According to World Development Indicators, in 1995, the infant mortality rate for Malawi was among the highest in the world, at 134.3 per thousand. This does not compare favorably with neighboring countries such as Zambia at 107.2, Tanzania at 91.6, or Zimbabwe at 52.8. Similarly grim was the child mortality rate, at 233.8 per thousand, which was substantially higher than neighboring Zambia's rate of 190.7. Chronic malnutrition is also a serious problem: 27 percent of children under the age of five are deemed to be underweight and 49 percent have stunted growth. The primary cause of these dismal figures is poor nutrition and lack of access to clean drinking water. In addition, the AIDS/HIV epidemic, which has led to absenteeism and loss of skilled manpower, has had a major effect on productivity.

Other factors external to the firm may also contribute to low labor productivity. Unreliable public utilities, such as electrical power disruptions, result in work stoppages and wasted time. Labor disputes and political upheavals may contribute to an unstable work environment. Even such seemingly simple factors as the government scheduling holidays in the middle of the week may encourage absenteeism. Suggestions were made to improve on productivity by declaring Mondays or Fridays as public holidays whenever the holidays fall in the middle of the week. This is important because the number of days not worked is already high by international standards. Finally, workers may be influenced by the cultural environment from which they come, with its own set of norms and standards that may be very different from those of a modern industrial sector. Firm managers complained often about the high rate of absenteeism and lack of respect for any work ethic.

On the other hand, low labor productivity may result more from factors within the firm. Much of Malawi's plant and equipment, for example, is old or obsolete by global standards. In other instances, low productivity may be attributable to poor management. Qualitative information from firms in Malawi indicates considerable under-investment in labor training and motivation. Training is generally perceived to be a government responsibility and a role for the private sector is viewed with skepticism because of a lack of bonding mechanisms and a propensity to poach skilled labor among firms.

8. Transportation

As a landlocked country highly dependent on overland movement of exports and imports, Malawi's transportation network and its connections to neighboring countries is of the utmost economic importance. While only one of the interviewed firms mentioned high transport costs as a constraint to conduct business, it is well-known that transport costs in Malawi are high.

Malawi has four major outlets: the northern corridor via Mbeya which gives access to the port of Dar Es Salaam; the Nacala corridor with access to Mozambique; the southern route to Beira also with access to Mozambique; and the southern route via Mwanza to Durban. Of all four, the Nacala corridor is the shortest (815km from Blantyre), and has the potential to be cheap, but is not the fastest. Until 1982, around 95 percent of Malawi's trade passed through Nacala and Beira, but throughout the 1980s and early 1990s the Mozambican civil war severely disrupted these vital trade routes, forcing most export and import traffic to be rerouted through distant ports in South Africa and Tanzania. The difficulty of transporting goods through Mozambique led the Southern African Development Community (SADC) to develop a northern transport route to link Malawi to the Tanzania port of Dar es Salaam in the 1980s. The $863 million project set up a route using Malawi's roads and lake transport and then linked these with the Chinese-built Tazara railway to the Tanzania capital. The northern route carried 15 percent of Malawi's trade in 1996, but its importance is expected to fade as the ports of Nacala and Beira return to their regular service. So far, however, the volume of freight being rerouted through Mozambique has been negligible.

Air freight

Air freight is extremely important for highly perishable nontraditional exports such as cut flowers, ornamental fish, etc.. Currently, air freight service is provided by 3 major airlines: Air Cargo, MK, which dealt exclusively with Lingadzi farm[16], and Dar Es. Other companies such as South Africa Airways, Kenya Airways, and Freight Air offer occasional freight services. All requests for providing an air freight service have to be submitted to Air Malawi, a public company of which Air Cargo is a subsidiary. Air Malawi has the power to approve or reject any application. Once approved, the company has to pay a seven percent of charter cost as a royalty to Air Malawi, thus offering an unfair advantage to Air Cargo. If the service is not permanent but ad hoc, then the royalty charges are four percent. These royalty charges, however, are always negotiable.

Air freight capacity exceeds demand by a large margin. Small operators, on the other hand, complain about Air Cargo's requirement of not accepting shipments smaller than one metric ton. At times, nontraditional exporters can only secure ½ metric ton. Private operators also complain of lack of reliable service between Nairobi International Airport and the European markets. While Kenya Airways is affiliated with KLM, some argue that the service in not of the same quality. For instance, Kenya Airways lands in Heathrow, which is not as well-connected as Amsterdam airport. Also, the reliability of flight schedules is another issue. When flights are delayed, firms are rarely notified and goods may be left unattended resulting in degradation of perishables. The fact that Kenya Airways does not land in Blantyre also creates problems. Exporters with European markets have to go through South Africa to Europe or ship from Lilongwe. Given the volume of trade by air, however, it may not be economically feasible to have a regular air freight service to Europe out of Blantyre. Also, because of the infrastructure, large aircraft with cargo capacity cannot land at Chileka airport.

Another issue raised by firms is the high cost of air freight. In high demand season, the freight cost is $2.20/kg for a palette that weighs about 2 tons, compared to $1.60/kg out of Nairobi. In addition, one needs to add the handling charge of MK1.00 /kg. During the low demand season, the freight charge varies between $1 and $1.5/kg.

Import and export procedures at the airport do not create too many problems. However, if a flight arrives after business hours, prior arrangements have to be made with custom officials so that goods can be cleared in a timely fashion.

Ocean Transport

Malawi mostly uses the ports of Nacala and Beira in Mozambique, and Durban in South Africa. Dar-es-Salaam is little used for a number of reasons. First, port costs are high. Second, the roads within Tanzania are in a poor state of repair. Third, the main road southward from the border with Tanzania is in poor condition.

[16] Since the time of the survey Lingadzi farm has closed down its business

Ocean shipping costs are relatively low compared with the cost of overland transport into Malawi. The exception is for imports made through Nacala. Shipment to Indian Ocean ports from FOB Western Europe is normally about US$25 per ton, and US$30 per ton from the Gulf. Shipments to Durban are now less costly than to Beira due to greater opportunity for vessels to obtain an outward load.

Rail Transport

A pressing issue is to decrease overland transport costs, especially since Malawi is a landlocked country. With 800 km of rail line, Nacala's corridor is the shortest route to the sea. However, railway routes in Mozambique sustained severe damage during the civil war and comprehensive rehabilitation on both sides of the border has been slow despite World Bank financing. At present, Mozambique and Malawi manage the railway line that is up for privatization. The idea is to have one operator for the entire corridor such that there would be no interruption of service. Currently, there is a change of locomotive that can take 1-2 hours at the border between Mozambique and Malawi.

Table 12 contains estimates of US dollar cost of transport from each of the main origins or ports. It can be seen that the cost of transport to Malawi's two main distribution centers (Lilongwe & Blantyre) from Nacala by rail and from Beira by road are similar, despite the fact that Nacala is near and that rail transport is usually cheaper than transport by road.

When compared with other rail rates in the region, the Nacala route is relatively expensive. In addition to the high per kilometer rail tariffs from Nacala, importers using this route face a number of further disadvantages compared with importation through Beira. Offloading and storage facilities at Nacala are very limited, with the result that any shipment greater than 3,000 tonnes is likely to result in delays and demurrage charges. This, in turn, means that shipments must be small and that the cost of shipment by sea is accordingly high. It is also not easy to arrange for a return load for transporters that deliver goods to Nacala. This also inflates the per ton cost using this route. Delays are also experienced due to the frequent shunting and stoppages for goods destined for Mozambique, which increases the time for the wagons to reach Malawi.

Table 12: Cost of Transport from Indian Ocean Ports

From	To	Distance (km)	Mode	Cost ($US/ton)	Cost/ton/km ($US)
Nacala	Blantyre	702	Rail	46	0.066
Nacala	Lilongwe	945	Rail	58	0.061
Beira	Blantyre	800	Road	50	0.063
Beira	Lilongwe	1,120	Road	60	0.054
Durban	Blantyre	2,315	Road	107	0.046
Durban	Lilongwe	2,635	Road	114	0.043
Johannesburg	Blantyre	1,727	Road	89	0.052
Johannesburg	Lilongwe	2,047	Road	98	0.048
Harare	Blantyre	604	Road	48	0.079
Harare	Lilongwe	924	Road	55	0.059

Source: MITCO

Road Transport

Within Malawi, roads are of average quality and the situation gets worse during the rainy season. Road maintenance fees are raised by revenues collected from the fuel tax (15 to 22 Tambala per liter, raised by the Petroleum Control Commission). Furthermore, there is a new fund with the European Union (EU), where the EU will add MK1.00 for each MK4.00 raised by the National Road Authority. Maintenance contracts are awarded competitively.

The disruption of service along the trade routes through Mozambique because of war has redirected most trade through the ports of South Africa. Although the longest distance (about 2700 km – 3800 km, depending on whether the traffic goes through Mozambique or Zambia), efficiency at the port of Durban more than compensates for the distance. Because of the poor state of roads, as noted above, and because of theft and vandalism, only about 15 percent of Malawi's trade passes through Tanzania.

Inland and regional transport is partly handled by a Malawian fleet, which faces increasing difficulties. During the Mozambique war, Malawi lost access to Nacala and needed additional trucks to ensure the transportation of goods to neighboring countries. At that time, the northern corridor through Tanzania was difficult to access. In an attempt to develop its own fleet of transporters, the Government of Malawi created a public institution that would serve as a broker between firms wanting to export or import goods and transporters. The government also provided other incentives: it issued a directive setting a transport rate of MK1.60 /ton-km, which was well above the real operating cost of MK1.00/k- ton. It also allowed spare parts for trucks to be imported duty-free. However, given that rates were much higher than those in neighboring countries, which averaged about MK1.10 /ton-km, the Malawian fleet was never able to successfully compete. At present, the Malawian fleet does not handle more than 40 percent of the volume of trade. Following the devaluation in 1998, however, the price set in 1994 of MK1.60 /km ton was believed to be too low.

Most road transport into and out of Malawi is by 30-ton truck owned by international transporters with headquarters in South Africa and Zimbabwe. Some of the larger Malawian transporters also operate internationally as well as domestically. A proportion of both international and domestic transport is commissioned through brokerage companies, but most of the importing and exporting firms deal directly with transporters, thereby eliminating the broker's margin of 15%.

With the aim of protecting domestic transporters from competition in the internal market, international transporters are required to deliver to warehouses on the main Blantyre/Lilongwe/Mzuzu artery. Should they deviate from this, they must pay an offloading or loading fee, which amounts to US$2-3 per ton. This raises the cost of distribution within Malawi since importers must either pay this fee or bear the cost of offloading and reloading onto a domestic carrier.

A greater volume of goods and commodities is imported into Malawi than is exported. This means that trucks bringing goods into Malawi must often return empty. The lack of backloads results in inward transport rates being well in excess of outward rates. Table 13 shows the published tariffs of a major transport broker for shipments to and from Lilongwe. It is seen that outward tariffs are only 46-65 percent of the inward tariff.

Table 13: Comparison of Outward and Inward Road Transport Tariffs

	To FOT Lilongwe ($US/ton)	**From FOT Lilongwe ($US/ton)**	**Inward as % of outward**
Beira	39	60	65
Johannesburg	46	107	43
Harare	26	58	46

Trucks travelling regionally are subject to heavy charges levied by the countries through which they pass. For example a 30-tonne truck transporting goods from Beira to Malawi would be subject to the Mozambican tolls, fees, and other costs shown in Table 14.

Clearly there is a case for a country to charge foreign vehicles for using its roads, since such vehicles, especially heavy trucks, place a burden on that country's transport infrastructure. However, the current Mozambican charges would seem excessive, and there seems little doubt that Mozambique is exploiting Malawi's landlocked situation for national gain. This is technically illegal and certainly not in the spirit of the SADC. There is a strong case for Malawi to raise the issue within the SADC framework.

Table 14: Mozambican Toll, Fees, and Other Costs for a 30 Ton Truck from Beira to Malawi

	$US
Port Fees	40
Round trip toll fee	250
Permit to operate in Mozambique	30
Insurance for one month	35
Immigration	10
Weighbridge expenses	20
Total	385
Total/ton	13

Export and import procedures

Other than the issues pertaining to duty-free access mechanisms, import and export procedures do not appear to create any particular problems. Exports are expedited within hours and non-contentious import shipments are cleared within 48 hours. Some delays may be encountered at border posts when documents have not been forwarded properly. The Mwanza border is the only one that is relatively well-equipped. It has telephones, a fax, and electricity. If some documents are missing, it is easy for the authorities to contact the firm or the freight forwarding agent. The other border posts lack communication equipment. For road transport, the authorization to proceed is given at the border, while the clearance and the settlement of all duties is done inland. Customs activities are still very much centralized in Blantyre. When a shipment is contentious, all matters are settled in Blantyre even if the port of destination is Lilongwe. Given the high amount of seizures or disputes arising from missing documentation and under-invoicing, it may take several months before matters are settled.

Other delays are reported with SGS inspections. Imports of FOB value equal to or in excess of US$2,000 are subject to pre-shipment inspection. The inspection ensures that a correct value is endorsed for import duty assessment on arrival of cargo. The importer gets the documents mentioned above and submits them to SGS with a copy of the clean report of findings to be issued with a Tax Assessment Notice (TAN), which is lodged at Customs.

The requirement for pre-shipment inspection by SGS is expensive for importers, demanding three percent of the value of the import as payment. Delays are experienced in the system, with importers having to pay for storage charges. There are doubts as to the effectiveness of the whole system, since inspections are not carried out when the goods arrive in Malawi, but are carried out in the country of origin.

Because of the need to improve tax and duty collection, the Government of Malawi with the support of multilateral agencies launched the Customs Reform Programme. The Programme was introduced in April 1995. The Mission Statement for the Department now aims at achieving the following:

- Collecting revenue through customs, surtax, and excise duties
- Facilitating legitimate trade and travel and upholding of laws relating to the import and export of prohibited and restricted goods
- Giving advice to Government on Customs and Excise matters
- Collecting and providing statistics on imports and exports

In order to further strengthen the Department of Customs and Excise, restructuring is underway to provide for more posts at all levels of the department. The principal elements of the restructuring exercise entail:

- Increasing the number of posts at all levels of the department so as to enhance supervision
- Providing better career prospects for Customs officers; this is essential for improving morale, which results directly in enhancing staff efficiency and effectiveness
- Providing short and medium-term specialized courses; in this regard, the Training center will be fully utilized for appropriate courses to address identified needs and skills shortages
- Reviewing customs systems and procedures in order to strengthen collection
- Re-developing infrastructure - a number of Customs offices and houses will be renovated, refurbished, and rehabilitated; the EU will provide about MK 45 million to the GOM to completely rebuild Mwanza Customs Station and renovate the Blantyre Collection Point, Chileka Customs Office, LIA Customs Offices, and Kanengo Collection Point; the Government of Malawi is also providing funding to build some new Chilumba offices

Construction of more staff houses at Mwanza, Chileka, and Karonga Customs stations using a portion of this same funding

- Providing more financial and material resources by adding a MK 50 processing fee on all Customs documents in addition to the funding from Treasury
- Establishing a National Revenue Authority (NRA), which has amalgamated the Departments of Customs and Excise and of Income Tax into a commercially oriented parastatal

Should all of the above be implemented, tax collection should be more efficient and customer oriented.

C. Other Pertinent Issues

While not addressed in the survey instrument, additional pertinent issues came up during the interviews. These included the problems facing small exporters and incentive schemes for regional markets.

1. Problems facing smaller exporters

It is generally agreed that export diversification takes place most easily in an environment that encourages small exporters to seek out opportunities for exporting new products to new markets in neighboring countries and overseas. Although small exporters may never account for the bulk of exports, their entrepreneurship in finding new opportunities can be critical to a dynamic and evolving export sector. Small exporters of nontraditional products in Malawi, however, are facing a wide range of bottlenecks:

- Small businesses can only export small quantities. Even when many combine their consignments, the volume of export rarely meets the tonnage requirement set for airfreight. When small exporters consolidate their exports for road transport via institutions such as Malawi Export Promotion Council (MEPC), they rarely can fill up a 20-foot container (14 tons), but nonetheless have to pay the full-load fee. There is a need for greater development of intermediation between producer and exporter.
- Small agricultural produce exporters usually do not have the necessary equipment to clean, sort, and package their goods. The state-owned marketing authority, ADMARC, has all the required storage facilities and machinery to sort and clean horticultural products. While access to these facilities is available on a fee basis, preference is reported to be given to those that sell their goods to ADMARC. Many are reluctant to form such a linkage due to the lower prices offered by ADMARC compared to those offered by private operators. This is an example of monopolistic behavior interfering in the development of market linkages.
- Small agricultural produce exporters need training in export documentation, quality control, how to negotiate a contract, and business management skills.
- Small exporters find it difficult to participate in international trade fairs since exporters have to pay their own fares to travel to these fairs. Instead, the people representing their interests, usually public officials, often do not have adequate knowledge and interest concerning their businesses. There is a need for alternative mechanisms to enable small exporters to enter into contact with potential importers.

- There is a need for greater coordination between institutions providing support to small exporters. For example, under the Government Preferential Purchase Programme (GPPP) and the Bulk Purchase and Distribution Programme (BUPAD), DEMATT mobilizes and trains small-scale producers and secures the materials for manufacture of acceptable quality commodities, which are supplied to central government stores. However, only a few urban businesses take advantage of the programs, and there is no effort to seek out export markets.
- Small exporters have little access to trade finance because of their limited collateral and banking experience. Lack of access to short and medium-term credit is a general problem facing SME's, but it is particularly acute in the export business because of the additional need for post-shipment credit.

2. Incentive schemes for regional markets

A major opportunity exists for Malawi to develop its exports to the Southern Africa regional market. Unlike many areas of sub-Saharan Africa, where the regional market is relatively small, the proximity of South Africa implies that the market for nontraditional exports within the region is very important. As a country where labor is abundant and wages are much lower than they are in South Africa, Malawi is well-placed to export labor-intensive products to that market. Although overland transport is expensive, transportation routes to South Africa are quite good. Furthermore, there is every evidence that South African investors are interested in establishing labor-intensive production in Malawi for export to South Africa, especially in view of the trade agreement that gives Malawi free access to the South African market.

In addition to South Africa, opportunities also exist in other countries of the region, such as Zambia, Zimbabwe, and Mozambique. The situation is complicated, however, by the existence of various bilateral trade agreements with these countries, by the ratification of the Trade Protocol of the Southern African Development Community (SADC), of which Malawi is a member, and by continuing negotiations at the international level under the World Trade Organization (WTO). Within Malawi, one hears frequent complaints from firms regarding unfair trade preferences favoring exporters in Zimbabwe. Inputs are said to be not taxed in Zimbabwe but are taxed in Malawi. It is not clear whether this is because the basic customs duty rates are different, which would support an argument for a customs union over a free trade area, or because Zimbabwe firms have access to duty exemptions on goods exported within the free trade zone, which is in violation of WTO agreements. There are also claims that the surtax is not paid on imports from Zimbabwe, which is in clear violation of the supposed neutrality of that tax. There is also the open issue of why Malawi has entered into a free trade agreement with a country that imposes various forms of quantitative restrictions that discriminate against Malawian goods.

All these issues require verification and further exploration. Furthermore, the SADC Trade Protocol will result in substantial changes in Malawi's trade tax regime and in its trade flows. The problem in Malawi and many other countries is that the private sector is not party to trade negotiations that will have a profound impact on local business. Too often the trade agreements are put in place, and only when the firms are hurt is there any awareness of what these agreements really entail. By the time the situation has been rectified, those that have been hurt have often gone under.

A related problem is a lack of understanding of how trade concessions are actually implemented. An example is the failure of customs officials to collect the surtax on imports from Zimbabwe. Too often, decisions made in the field are influenced more by who is willing to pay than by the way in which the rules are supposed to be applied. This is especially true when the rules are at all ambiguous.

V. CONCLUSIONS AND POLICY RECOMMENDATIONS

A. Infrastructure

Unreliable and costly utilities were by far the most critical obstacle cited by firms. With the advent of the technological revolution, telecommunication is the core of the information infrastructure needed by each country to participate and compete in the global economy. Similarly, a reliable energy supply is vital for development and promotion of the private sector. In addition to severely constraining the performance of existing firms, poor infrastructure acts as a deterrent to foreign direct investment, which is sorely needed in Malawi. Empirical evidence suggests that the overall quality of available infrastructure is increasingly becoming the overriding factor in attracting foreign investment. Consequently, it is crucial to improve the delivery of these services. This will require further liberalization and new investments.

With regard to the telecommunications sector, the major need for private business is to increase the development of wireless communications by a competitive private sector and to link that with the existing cable network. This will require complete liberalization of wireless communications and investment by MPTC in the hardware and software required for linkage. It will also require implementation of the Communications Act of 1998, which allows for the establishment of a regulatory authority separate from MTPC. This should facilitate the creation of an enabling environment for technology innovation and competition and thereby allow new entrants and operators into the communication industry. These developments should lead to improvements in the quality and the prices of services delivered.

The passage of the Electricity Act enabling private investment in power distribution is also a step in the right direction. Consideration should be given to do the same with the generation of power. This would allow private investors to invest in alternative sources of energy. To ensure fairness in competition, it is essential to set up a regulatory body to oversee the sector that is separate from any public investment in or operation of power generation and distribution facilities. Equally important, utility suppliers should be able to charge prices that reflect the cost of production and distribution.

Malawi should be linked with the grid of the Southern Africa Power Pool, of which it is a member. This would do much to enhance power availability and to lower costs. Such a linkage raises a number of issues, which need to be analyzed and debated in public:

- The extent to which Malawi is willing to be dependent on external sources of power
- How power distribution from this source can best be organized and regulated
- How this distribution should be linked with the distribution of locally generated power

- What price Malawi should pay for this electricity
- What rate structure should apply to Malawi's users

B. Macroeconomic Mismanagement and the Exchange Rate Regime

Macroeconomic mismanagement is a major problem, and one high on the list of complaints by the private sector. Persistent fiscal deficits, coupled with a wobbly exchange rate policy, have resulted in an unstable and at times substantially overvalued exchange rate. High expectations of inflation and the government's need for financing have led to high and fluctuating interest rates. All of this has made planning difficult and strongly discouraged new investment.

The major need is to control public expenditures and to develop a tax system that can pay for these expenditures without strongly discouraging the private sector. Except for a few recommendations regarding tax exemptions for inputs used in the production of exports, the area of macroeconomic management lies largely outside the scope of this study. However, the exchange rate is one dimension of macroeconomic management that is so critically important to the private sector that it is considered here.

One of the factors resulting in overvaluation of the kwacha is government fiscal deficits, leading to inflation in the presence of either a fixed exchange rate or pressures to constrain the rate of depreciation of the nominal rate. This biases the allocation of resources away from the export sector, because of low export prices measured in terms of local currency, and it encourages measures to protect against imports, which in turn further distorts resources and encourages rent-seeking behavior. In addition, periodic devaluation and changes in management of the exchange rate result in substantial instability in both the nominal and the real exchange rate, creating enormous uncertainty for producers and investors.

There are a number of areas that need to be examined in greater detail in order to understand the workings of the foreign exchange market. These include:

- Ways in which foreign exchange is implicitly rationed during periods of overvaluation, contributing to import protection, rent-seeking, and a bias against exports. This might be through foreign exchange retention requirements, informal credit controls affecting importers, pressures on the parallel market for foreign exchange, and other methods that can be highly detrimental to trade. These factors need to be studied and publicized to place pressure on government by exporters and other stakeholders to avoid overvaluation.
- Linkages between fiscal policy, monetary policy, debt management, and exchange rate management. Frequently, the central bank is only vaguely aware of how its various policies are affecting the real exchange rate. Maintaining a stable and appropriate real rate of exchange is not high on its list of targets. Yet this is the most important macroeconomic variable for producers. These interactions need to be explicitly modeled.

Management of the exchange rate in the face of an economy highly dependant on climatic conditions, with underdeveloped financial markets and a narrow export base should be a major priority. If the exchange rate is allowed to float, external disturbances can have a profound impact on the exchange rate, and on the profitability of exports, especially nontraditional exports that normally have relatively low profit margins. If the central bank tries to mitigate these effects through the buying and selling of foreign exchange, on the other hand, it runs the risk of losing reserves and the confidence of the public, resulting in speculative pressures being added to external forces.

C. High Cost and Lack of Availability of Finance

Macroeconomic mismanagement has given rise in Malawi to very high interest rates, partly because of expectations regarding future rates of inflation and partly because the government has tended to crowd the private sector out of capital markets. Even when real rates of interest measured relative to inflation are not very high, potential borrowers are frightened by high nominal rates alone, decreasing the propensity to invest and to borrow working capital when needed. Both the high cost and limited availability of finance were cited as major factors constraining the private sector. As a result, the majority of firms surveyed reported financing their working and long-term capital through internally generated funds. Improving macroeconomic management should lead to lower borrowing costs for the private sector.

In addition to high nominal rates of interest, lack of competition among financial institutions results in high margins between borrowing and lending rates. Part of this problem is also due to the fact that most financial institutions are tied directly or indirectly to the state. There is a need for liberalization of the banking sector, promotion of greater competition within the sector, and establishment of more non-bank financial institutions. Especially important are institutions that are able to mobilize long-term savings such as insurance and pension funds. Also important is the creation of specialized institutions that can service the SMEs, especially those requiring export financing.

A useful study would involve separation of the high cost of finance that is due to macroeconomic mismanagement, including inflation and the crowding out effect, from that related more to the fundamental nature of weak financial institutions and problems inherent in the inappropriateness of commercial banks, with their short-term liabilities, providing substantial amounts of medium and long-term capital.

D. Security

The security issue is not an easy one to handle. However, threats to personal safety and property thefts can have a long-term detrimental effect on the investment climate of the country. This has a potentially devastating impact on the rural economy, where some services such as banking and distribution of goods are being withdrawn based on security concerns.

The current government effort to tackle the rise in criminality by increasing the level of available resources to support law enforcement officers, including the police and the judiciary, should be encouraged. Also, lessons could be learned from countries that have dealt with similar problems, such as South Africa. Ultimately, of course, solving the problem of security depends on solving the problem of poverty.

E. Sector Linkages

This report has highlighted the lack of strong linkages between sectors of the economy – whether they be agriculture viz industry, formal viz informal, or large firm viz SME. In Malawi, the SME and informal sector appears to be less well developed than in many other African countries. Certainly, its linkages with the formal sector are weak, perhaps because of the way in which the formal sector was dominated by a conflux of strong political and business interests for so many years, which allowed few opportunities for entry of small and medium firms. Today, this lack of linkages is often expressed by managers of firms in the formal sector in terms of the unreliability of input supply and the rising cost of raw materials. This is a serious problem in view of the finding cited that economic growth occurs largely from the expansion of larger firms, with benefits spreading more broadly through their hiring and through their linkages with other, smaller firms. Thus lack of linkages can be very detrimental to growth with equity in Malawi.

There is need to study the linkages between industry-agriculture, formal-informal, large firm-SME sectors in order to understand what the barriers are that impede the development of these linkages and how these can be overcome. Of particular importance are the ways in which workers move from the farm to working in the formal sector and whether the formal sector could draw more on experience gained in the informal sector, or whether it is just better to start from scratch. Also important is the extent to which there are input-output flows between the two sectors, as opposed to the formal sector buying its inputs from abroad, and how these input-output linkages could be strengthened. What is the feasibility of "putting" out arrangements, as are often used in the garment sector for cut-make-trim operations? Can the informal sector provide services, such as cleaning and maintenance. How can the formal sector rely more on small farmers to provide its inputs? Another important question is whether the informal sector benefits from trade credit provided by the formal sector as a source of capital and how this linkage could be strengthened.

F. Trade and Other Indirect Taxes

Other major problems, which showed up to some extent in the survey but have been documented more fully elsewhere, are associated with trade and other indirect taxes and the concessions that have been or are likely to be granted in various national, bilateral, and multilateral agreements. Incentive mechanisms such as industrial rebate and duty drawback need to be drastically simplified as few eligible firms are able to benefit from them. Since the margins are increasingly getting smaller due to stiff competition on the international market, it is essential to offer adequate tax incentives consistent with practice in competing countries. One of the most important of these is workable mechanisms for providing tax-free access to inputs used in the production of exports.

It is evident that the various schemes in Malawi for granting exemption on indirect taxes paid on inputs used in the production of exports work very imperfectly. The rationale behind the Industrial Rebate Scheme is unclear. It does not offer an incentive to export. The scheme also favors larger over smaller producers, a particular problem for smaller exporters. The Duty

Drawback and Surtax Schemes are appropriate in their incentive structures but do not work well administratively. The only scheme that does work reasonably well is the Export Processing Zone/Bonded Warehouse Scheme, but this is clearly also biased against smaller firms. None of the schemes effectively allows for exemption on taxes paid on inputs that are produced locally but are subsequently incorporated into products that are exported.

What is needed, as noted above, is a program that estimates the tax content of exports based on a set of coefficients and provides either immediate payment for these taxes or offers a negotiable credit against payment of other taxes. Immediate payment will require some sort of revolving fund. Experience with these is not very good since the funds tend to become depleted. A better option is a negotiable tax credit, which can either be used by the exporter in lieu of other tax payments or sold on the open market.

At the regional level, there is a major need to analyze the various bilateral and multilateral trade agreements to see (1) how they are currently implemented in practice, (2) how they are likely to evolve in the future, (3) how this will affect the competitiveness of Malawian industry, and (4) what should be Malawi's position in these trade negotiations. This analysis would measure the impact of the existing structure of trade and other indirect taxes on incentives facing firms, using tax rates based on actual taxes collected rather than official tax rates. The analysis should investigate how these incentives are changed by existing trade agreements with Zimbabwe and South Africa and whether these agreements are in conformance with WTO standards and are in Malawi's best interest. The analysis should also examine the impact of the SADC Trade Protocol on the structure of incentives facing producers in Malawi, as well as the effects of changes introduced by the agreement between the European Union and the ACP countries (African, Caribbean and Pacific). The results should be discussed widely with the private sector so that they can have input into trade negotiations involving Malawi before agreements are made.

G. Workforce Development

Malawi is a very poor country with one of the lowest per capita incomes in the world. This would seem to be a reason why firms could take advantage of low-wage rates in order to produce and export labor-intensive goods, such as garments, to the world market. In fact, however, firms claim that they have substantial problems in hiring and retaining workers who are reliable and capable of upgrading their skills. Absenteeism is high and very elementary industrial skills are frequently lacking.

On the other hand, our survey suggests that there is considerable under-investment in labor. For firms, labor training is generally perceived to be a government responsibility and corporations are reticent to train labor due to their inability to retain the workers after they are trained. This is especially unfortunate because recent experience elsewhere in Southern Africa emphasizes the importance of intimate involvement of the private sector in industrial training.

A study should be undertaken to identify the reasons why industrial labor productivity is very low in Malawi. This study should distinguish between (1) outdated plant and equipment, (2) external factors such as interruptions in electrical power, (3) lack of good organization and work practices due to weak management, and (4) weaknesses of the work force due, for example, to poor health or insufficient experience and education. A pilot effort along the general lines of the Botswana scheme noted above should also be undertaken to test an industrial training program in which firms and business associations are heavily involved in ascertaining training needs, development of curricula, etc. In this respect, the Center for Human Capacity Development, Global Bureau, USAID/Washington has recently funded an effort to develop a Program in Workforce Development, which has been tested in a number of countries all over the world.[17]

Lack of skilled labor is often dealt with by hiring foreign expertise. All firms making use of expatriates in our survey denounced the TEPs system as being overly cumbersome. While the effort of the Malawi Government to create more jobs for its skilled labor force is laudable, restrictions on the issuance and renewal of TEPs should be minimal. Foreign expertise usually brings know-how, contacts, and ready sources of finance. This can potentially lead to new investment, with increased production and thus employment. The latter would largely offset the few skilled positions forgone by hiring foreign workers.

H. Transportation

The report highlights the many problems experienced in the transportation sector. While not generally considered to be critical by the private sector, they are nonetheless thought to be important. The following is a set of recommendations emanating from this section of the report:

- The rehabilitation of the physical infrastructure and the streamlining of the management of the rail link with Nacala in Mozambique would substantially reduce the cost of transport to the sea. This should have high priority.
- Air Cargo should be placed on an equal footing with other airlines insofar as freight rates and other charges are concerned.
- Charges for road transport should be deregulated, and restrictions on foreign transporters should be lifted. Malawi needs highly competitive and low-cost transportation to neighboring countries and the sea to offset its geographical location.
- Negotiations on transportation rates in neighboring countries should be pursued within SADC to lower these rates for Malawian goods.
- A study should be conducted of the transport sector to determine the weight of taxes in transport costs, and whether these taxes could be reduced without decreasing revenues if, for example, the reduction contributed to an increased volume of transport activity.

I. Final Remarks

The survey and analysis of this report should be considered as exploratory. The sample was too small and the resources were too limited to explore all the questions raised in Section III. The main virtue of the study, however, is that it asks the private sector what it thinks are its major constraints, prioritizes these and measures their magnitude to the extent possible, analyzes the most important of these constraints, and recommends ways in which they might be overcome.

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[17] "Investing in Tomorrow's Workforce", prepared by the Center for Workforce Development, Education Development Center, Inc., 1998.

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